SERBA WANGI (PG) SDN BHD v. KETUA PENGARAH HASIL DALAM NEGERI

HIGH COURT MALAYA, PULAU PINANG
KENNETH ST JAMES J
[CIVIL APPEAL NO: PA-14-1-03-2021]
16 FEBRUARY 2025

Abstract – *(i) For the purpose of claiming a reinvestment allowance under Schedule 7A of the Income Tax Act 1967, 'processing' does not require a change in the fundamental 'structure'. Instead, 'processing' encompasses activities that subject goods to a series of systematic actions, resulting in a product with a higher market value than the original raw material. This includes activities that physically change the raw material into different products, even if the basic structure remains similar. The definition of processing provided by the Inland Revenue Board, in its own rulings, should be used when interpreting the law; (ii) Reinvestment allowance in the Act was implemented for the very purpose of encouraging companies to expand, modernise and automate their businesses, to increase their production capacities. As such, the provisions of Schedule 7A should be interpreted purposively and not restrictively.*

REVENUE LAW: *Income tax – Reinvestment allowance – Taxpayer company spent money to enhance business in activity of processing – Taxpayer applied for reinvestment allowance ('RA') – Inland Revenue Board refused taxpayer's claim for RA – Taxpayer's appeal to Special Commissioner of Income Tax unsuccessful – Whether taxpayer satisfied requirements to get RA – Whether taxpayer carried out project of 'expanding, modernising or automating its existing business' in respect of 'processing' product – Whether diversified its range of products – Whether taxpayer entitled to RA – Income Tax Act 1967, Schedule 7A*

WORDS & PHRASES: *'processing' – Revenue law – Income tax – Reinvestment allowance – 'processing is the subjection of goods to a process which means, goods or materials are subjected to a process which falls short of the manufacturing of a new article and involves the treatment of the goods in some way, other than natural growth' – 'processing refers to a technique of preparation, handling or other activity designed to affect a physical or chemical change in an article or substance' – 'an activity may be termed as processing where a product has gone through a series of actions that are systematic, has a higher value than before (has been made more marketable and would attract a higher price for the same amount) and accepted by the market' – Inland Revenue Board's Reinvestment Allowance Ruling No. 6/2012, para. 6.2.2*

The appellant was incorporated in 1995. Prior to 2006, the appellant operated its business in a rented factory premises. The appellant constructed its new factory in 2006 and, in 2007, applied for a reinvestment allowance ('RA') on the building costs for the new factory, in the amount of RM5,240,857, and the purchase of new machinery, in the amount of RM2,814,247, for the year of assessment ('YA') 2006. In 2012, after a visit and an audit at the appellant's new factory, the Inland Revenue Board ('IRB') informed the appellant that: (i) the appellant was not permitted to claim 100% RA for the building costs of the new factory. The IRB would allow only part of the RA application, *ie*, for the building costs of the additional area of the new factory over the original area of the previously rented factory; and (ii) the RA claim for the new machinery was allowed. The appellant explained to the IRB that before YA 2006, the appellant was a rice wholesaler and, in 2006, it diversified into the business of processing rice; as such, the appellant was entitled to the whole RA claim for the building cost of the new factory. The IRB rejected the appellant's whole RA claim, as it was of the opinion that the appellant only started rice processing in 2006 and, thus, had been in operation for less than 12 months. The IRB disallowed the appellant's whole RA claim. The appellant had to pay RM21,012.24 for YA 2007 and RM542,505 for YA 2008. The appellant's appeal to the Special Commissioner of Income Tax ('SCIT') was unsuccessful as the SCIT was of the opinion that, *inter alia*, (i) the appellant did not satisfy the requirements to get the RA, *ie*, the appellant had not carried out a project of 'expanding, modernising or automating its existing business' in respect of 'processing' a product and had not diversified, *ie*, increased or changed its range of products; (ii) there was no evidence that the appellant's machinery sorted out the rice grains as the sorting did not change the structure of the rice grains. As such, the appellant did not satisfy the processing requirement under para. 8(a) of Schedule 7A to the Income Tax Act 1967 ('Act'); and (iii) since the appellant held a wholesale licence, it could not be processing rice or be allowed to process rice. The appellant could only be a rice wholesaler and, if the appellant did not have a licence to process rice, it could not be entitled to an RA for expanding its factory and purchasing machinery for the business of rice processing. Hence, the present appeal.

Held (allowing appeal):

(1) To be entitled to the RA, it must be proven that the appellant: (i) had been in operation for not less than 12 months; (ii) had spent money on a factory or machinery for the purpose of qualifying project, which is a project to expand, modernise or automate its existing business, in manufacturing or processing a product or related product in the same industry; and (iii) alternatively, had spent money on a factory or machinery for the purpose of a project to diversify its existing business into any related product within the same industry. (para 23)

(2) The SCIT did not indicate the authority or, at least, the reference that instructed them to find that, when an activity did not change the structure of the rice grains, the activity could not be considered to be the required 'processing' activity under para. 8(a) of Schedule 7A to the Act. The IRB's Reinvestment Allowance Ruling No. 6/2012, in para. 6.2.2, provided definitions for 'processing' which included: (i) 'processing is the subjection of goods to a process which means, goods or materials are subjected to a process which falls short of the manufacturing of a new article and involves the treatment of the goods in some way, other than natural growth'; (ii) 'processing refers to a technique of preparation, handling or other activity designed to affect a physical or chemical change in an article or substance'; and (iii) 'an activity may be termed as processing where a product has gone through a series of actions that are systematic, has a higher value than before (has been made more marketable and would attract a higher price for the same amount) and accepted by the market'. The SCIT had seriously misdirected themselves that the appellant did not carry out the activity of 'processing' which led the SCIT to erroneously deny the appellant's claim for an RA. The RA was allowed for 'processing'. (paras 28, 30, 31, 33 & 37)

(3) Evidence disclosed that the appellant's business and, by extension, the machinery that the appellant purchased, for which it was claiming an RA, was to turn raw rice into three products: (i) processed rice (for household consumption); (ii) broken rice (supplied to factories that make noodles, like vermicelli); and (iii) rice bran (sold as animal feed). The appellant's machinery systematically subjected the raw rice to a series of actions that physically changed the raw rice into these three products which, when taken together, had a higher value than the raw rice in its original form. It was clear and undoubtable that the appellant carried out the activity of 'processing'. Further, the appellant 'expanded' its business by building a factory that was larger than its previously rented factory premises. The appellant 'automated' its business by purchasing machinery, such as the various sorter machines, thus reducing human effort, to process the raw rice into the three different products. (paras 34-36)

(4) The SCIT placed a higher than necessary burden of proof on the appellant when the SCIT required the appellant to prove that its business or its machinery changed 'the structure of the rice', citing the example of turning paddy into rice, before the SCIT would accept that the appellant performed the required activity of 'processing' rice to be entitled to make an RA claim. The SCIT should have, instead, simply considered whether the appellant turned the raw rice into another form, *ie*, into another product. That would have sufficed to hold that the appellant carried out the processing of rice. (paras 38 & 39)

(5) The SCIT arrived at its grounds through a serious misdirection and misapplication of the law on evidence because the SCIT ignored all the other relevant evidence. The SCIT disregarded the evidence that: (i) the appellant clearly incurred capital expenditure to acquire two Yamatech Grain Colour Sorter Double Sensor machines ('Yamatech machines'); and (ii) both the Toyo Super Coloured Grain Sorted (Double Sorting Type) machines and the Yamatech machines performed the same function, which was to sort and clean the raw rice; and (iii) the appellant had been in operation for longer than 12 months before YA 2006. (paras 53, 55 & 56)

(6) The appellant's wholesale licence was governed by the Control of Padi and Rice (Licensing of Wholesalers and Retailers) Regulations 1996 where the appellant was particularly subjected to the duties of a wholesale licensee, as set out in regs. 8 and 9. While regs. 8 and 9 obligated the appellant to perform certain duties and prohibited the appellant from performing certain acts, they did not prohibit the appellant from operating a rice-processing business. Therefore, there was no basis in law for the SCIT to have found that the appellant could not be allowed to carry out rice-processing and hence, could not be given the RA claimed because the RA related to a prohibited activity. (paras 64-66)

(7) The SCIT's deciding order was set aside and the IRB's assessments concerned were discharged. The penalty amounts of RM21,012.24 for YA 2007 and RM542,505 for YA 2008, which were already paid over by the appellant to the IRB, were ordered to be returned by the IRB to the appellant. (paras 70 & 71)

Case(s) referred to:

Chua Lip Kong v. Director-General Of Inland Revenue [1981] CLJU 157; [1981] 1 LNS 157 ***(refd)***

Director-General Of Inland Revenue v. Rakyat Berjaya Sdn Bhd [1984] 1 CLJ 219; [1984] 1 CLJ (Rep) 108 FC ***(refd)***

Ketua Pengarah Hasil Dalam Negeri v. Classic Japan (M) Sdn Bhd & Another Appeal [2021] 5 CLJ 86 HC ***(refd)***

Ketua Pengarah Hasil Dalam Negeri v. Tenaga Nasional Bhd [2024] 8 CLJ 301 CA ***(refd)***

Tenaga Nasional Bhd v. Ketua Pengarah Hasil Dalam Negeri [2022] 7 CLJ 285 HC ***(refd)***

Legislation referred to:

Control of Padi and Rice (Licensing of Wholesalers and Retailers) Regulations 1996, regs. 8, 9

Income Tax Act 1967, ss. 112(3), 113(2), 133A, Schedule 5 paras 23, 34, 39, Schedule 7A paras. 1(a), 8(a), 9

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For the respondent - Siti Salina Hassan & Ariffuddin Shahrulzani; Inland Revenue Board

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JUDGMENT

Kenneth St James J:

Prelusion

[1] Under the Income Tax Act 1967 (ITA), the appellant applied for a reinvestment allowance (RA). The appellant is a Malaysian company-taxpayer. Where a Malaysian company-taxpayer has spent money to enhance its business in the activity of processing its product, it is entitled to be given an RA. The RA is 60% of the money spent for this purpose.

[2] The respondent (IRB) refused the appellant's claim for an RA. The appellant appealed to the Special Commissioners of Income Tax (SCIT). The SCIT dismissed the appellant's appeal. The appellant appeals to the High Court.

[3] Should the appellant's appeal be allowed, *ie*, it should be given the RA it has asked for? Or should the appellant's appeal be dismissed, *ie*, it should not be given the RA?

The Pertinent Statutory Provisions

[4] I first set out the provisions of the ITA pertinent to this appeal. Section 133A of the ITA provides for special tax reliefs (an allowance) to be given to a company-taxpayer who spent money investing in its business. The allowance which is the subject of this appeal is the RA, which is set out in Schedule 7A of the ITA.

[5] Schedule 7A provides that where a company-taxpayer spends money (called a "capital expenditure") on a "factory" or on "machinery" for a "qualifying project", the company-taxpayer must be given an RA of 60% of the money so spent.

[6] A "qualifying project", which mandates the RA to be given to the company-taxpayer, is a project for "expanding, modernising or automating its existing business" concerning "processing" a product or "any related product in the same industry". A qualifying project is also a project for "diversifying its existing business into any related product within the same industry".

[7] Section 133A and the pertinent portions of Schedule 7A are set out below for reference (with my emphases added). The parties agree that these are the applicable words of s. 133A and Schedule 7A at the time of the appellant's appeal to the SCIT and in this appeal:

> **Section 133A. Special incentive relief.**
>
> Notwithstanding any other provisions of this Act, *special incentive relief shall be given in accordance with Schedule 7A* and Schedule 7B.

SCHEDULE 7A: Reinvestment Allowance

[Section 133A]

Reinvestment Allowance

1. Subject to this Schedule, *where a company* which is resident in Malaysia:

(a) has been in operation for not less than twelve months; and

(b) has incurred in the basis period for a year of assessment *capital expenditure on a factory, plant or machinery* used in Malaysia *for the purposes of a qualifying project referred to under subparagraph 8(a)*;

there shall be given to the company for that year of assessment *a reinvestment allowance of an amount equal to sixty per cent of that expenditure*:

Provided that such expenditure shall not include capital expenditure incurred on plant or machinery which is provided wholly or partly for the use of a director, or an individual who is a member of the management, or administrative or clerical staff.

8. In this Schedule, *"qualifying project" means*:

(a) *a project undertaken* by a company, *in expanding, modernizing or automating its existing business in respect of* manufacturing or *processing-[please see Note below]-of a product or any related product within the same industry or in diversifying its existing business into any related product within the same industry*; …

(Note: The 2009 amendments to the ITA removed the words "or processing". But it is the ITA provisions before the 2009 amendments which are applicable to this appeal. This appeal relates to the provisions of the ITA in YA 2006, YA 2007 and YA 2008, relating to the activity of "processing". This is not in dispute between the parties. The parties agree that for this appeal, the activity of "processing" a product or a related product within the same industry, has to be considered.)

9. In this Schedule:

"automating" refers to *a process whereby manual operations are substituted by mechanical operations with minimal or reduced human intervention*: …

"diversifying" means *to enlarge or vary the range of product* of a company *related to the same industry*; …

"expanding" refers to *an increase of a product capacity or expansion of factory area*; …

"manufacturing" means:

(a) conversion by manual or mechanical means of organic or inorganic *materials into a new product by changing the* composition, *nature or quality of such materials*; …

"modernizing" means an upgrading of manufacturing equipment and process; …

(emphasis added)

Pertinent Chronology Of Facts And Proceedings

[8] I next set out a chronology of the pertinent facts and proceedings for this appeal:

(i) 1995 (27 November 1995) – the appellant was incorporated.

(ii) before 2006 – the appellant operated its business in a rented factory premises.

(iii) 2006 – the appellant constructed its new factory.

(iv) July 2007 – the appellant applied for an RA on the building costs for the new factory (RM5,240,857) and the purchase of new machinery (RM2,814,247), for the year of assessment (YA) 2006.

(v) February 2012 (five years later) – the IRB visited the appellant's new factory and conducted an audit.

(vi) April 2012 (16 April 2012) – the IRB issued a letter to the appellant stating that:

(a) the appellant is not permitted to claim 100% RA for the building cost of the new factory. The IRB would allow only part of the RA application, *ie*, allow RA only for the building cost of the additional area of the new factory over the original area of the previously rented factory; and

(b) the RA claim for the new machinery is allowed.

(vii) 27 April 2012 – the appellant responded, through its tax agent, explaining to the IRB that before YA 2006, the appellant was a rice wholesaler, and in 2006, it diversified into the business of processing rice. As such, the appellant is entitled to the whole RA claim (for the building cost of the new factory).

(viii) June 2012 (19 June 2012) – the IRB responded and rejected the appellant's whole RA claim, citing the reason that the appellant only started rice processing in 2006. As such, it has been in operation for less than 12 months.

(ix) July 2012 (2 July 2012) – the appellant's tax agent then clarified with the IRB that the appellant had been in the rice processing business for more than eight years before 2006, and should be given the RA under Schedule 7A and s. 133A of the ITA. The appellant's tax agent produced the invoices and supporting documents for the purchase of rice processing machinery (two colour grain sorters in 2002 and two-grain colour sorters in 2005).

(x) 16 July 2012 – the tax agent wrote further to the IRB to enclose related documentary evidence of the purchase of the two grain sorters, including a brochure for such machinery.

(xi) November 2012 (19 November 2012) – the IRB wrote again to wholly reject the appellant's RA claim, giving the ground that the two-colour sorters merely sort out foreign objects in the rice, which does not qualify as rice processing, for claiming an RA.

(xii) 27 November 2012 – the IRB then issued its Form NL to the appellant, disallowing the whole RA claim, and its Form JA (notice of additional assessment/penalty) for YA 2007 and YA 2008. The appellant had to pay RM21,012.24 for YA 2007 and RM542,505.26 for YA 2008.

(xiii) April 2015 (12 April 2015) – the appellant appealed to the SCIT against the IRB's Form NL and Form JA by filing Form Q for YA 2006, YA 2007 and YA 2008.

(xiv) October 2017 – the trial before the SCIT.

(xv) March 2018 (27 March 2018) – the SCIT dismissed the appellant's appeal.

(xvi) April 2018 (9 April 2018) – the appellant lodged this appeal to the High Court against the SCIT's decision.

The Law On Appellate Intervention In Appeals From The SCIT

[9] Foremost, it is beneficial for me to set out the law (the legal principles) for appellate intervention in appeals from the SCIT. I will first look at the pertinent provisions in the ITA and next look at the case law.

Legislation – The Provisions Under Schedule 5

[10] One – para. 23 of Schedule 5 of the ITA provides that the SCIT's decision is final, subject only to the other provisions of Schedule 5. Schedule 5 is about appeals to and from the SCIT.

[11] Paragraph 23 of Schedule 5 is set out below for reference (with my emphases added):

> Deciding orders
>
> 23. As soon as may be after completing the hearing of an appeal, **the Special Commissioners shall give their decision on the appeal** in the form of an order which shall be known as a deciding order and **which, subject to this Schedule, shall be final**.
>
> (emphasis added)

[12] Two – para. 34 of Schedule 5 of the ITA provides that parties can appeal against the SCIT's decision on a question of law.

[13] The pertinent portion of para. 34 of Schedule 5 is set out below for reference (with my emphases added):

> Appeals to the High Court
>
> 34. (1) **Either party to the proceedings before the Special Commissioners may appeal to the High Court on a question of law** against a deciding order made in those proceedings.
>
> (emphasis added)

[14] Three – para. 39 of Schedule 5 of the ITA provides that on appeal from the SCIT to the High Court, the High Court must determine any question of law. The High Court can order the assessment to be "confirmed, discharged or amended", or remit the case to the SCIT, or make such other order as the High Court thinks "just and appropriate". This provision places a duty on the High Court, on an appeal from the SCIT, to make a "just and appropriate" determination. In other words – to do justice.

[15] Paragraph 39 of Schedule 5 is set out below for reference (with my emphases added):

> 39. *The High Court shall hear and determine any question of law arising on an appeal under paragraph 34 and may* in accordance with its determination thereof:
>
> (a) order the assessment to which the appeal relates to be confirmed, discharged or amended;
>
> (b) remit the appeal to the Special Commissioners with the opinion of the court thereon; or
>
> (c) *make such other order as it thinks just and appropriate.*
>
> (emphasis added)

Case Law

[16] The IRB cites the often-quoted 1981 Privy Council case of *Chua Lip Kong v. Director-General Of Inland Revenue* [1981] CLJU 157; [1981] 1 LNS 157; [1982] 1 MLJ 235; [1981] 1 MLRA 757 – to submit that, on appeal, the High Court cannot interfere with the SCIT's findings of primary fact. (A finding of primary fact is the SCIT's finding of fact made from direct evidence, *ie*, from the oral and documentary evidence produced in the trial before it. In other words, the SCIT makes a finding of primary fact without having to make any inferences from the evidence produced).

[17] The IRB argues that I am to treat this appeal from the SCIT differently to a normal civil appeal from the subordinate courts. The IRB argues that in an appeal from the SCIT, I cannot overturn the SCIT's findings of fact. Put differently, I am restricted to only the questions of law that arise in this appeal.

[18] The IRB refers me to this well-known extract from *Chua Lip Kong* (*supra*) at MLJ p. 236:

> Their Lordships cannot stress too strongly how important it is that, in every Case Stated for the opinion of the High Court, the Special Commissioners should state clearly and explicitly what are the findings of fact upon which their decision is based and not the evidence upon which those findings, so far as they consist of primary facts, are founded. **Findings of primary facts by the Special Commissioners are unassailable. They can be neither overruled nor supplemented by the High Court itself**; ..
>
> (emphasis added)

[19] However, to my mind, this submission – that on appeal to the High Court, the SCIT's findings of fact cannot be overturned – cannot be a blanket, unqualified prohibition. It cannot be the case that any and every finding of fact is "unassailable" – no matter how misdirected, or no matter whether there was evidence to justify the finding of fact, or no matter whether the legal tests and principles were applied erroneously.

[20] I find support for my view in the case law authorities. I am instructed by case law authorities that on appeal to the High Court, the High Court can and should interfere and correct the SCIT's decision, even their findings of fact – so as to make a determination that is just and appropriate:

(i) if the SCIT had misdirected themselves in law;

(ii) if there was no evidence to justify their findings of fact;

(iii) if they disregarded the relevant evidence;

(iv) if they had made incorrect assumptions of the legal effect or consequences of their findings of fact, particularly if they had drawn inferences to make their findings of fact; or

(v) if they had misapplied the relevant law, such as misinterpreted the law.

[21] I will cite two case law authorities that led me to this conclusion. First – the Privy Council case of *Chua Lip Kong* (*supra*) itself, at MLJ p. 236:

> *From the primary facts admitted or proved the Commissioners are entitled to draw* inferences; such inferences may themselves be *inferences of pure fact, in which case they are as unassailable as the Commissioners' finding of a primary fact; but they may be, or may involve* (and very often do), *assumptions as to the legal effect or consequences of primary facts, and these are always questions of law upon which it is the function of the High Court* on consideration of a Case Stated *to correct the Special Commissioners if they can be shewn to have proceeded upon some erroneous assumption as to the relevant law*.
>
> (emphasis added)

[22] Second – the 1983/1984 Federal Court case of *Director-General Of Inland Revenue v. Rakyat Berjaya Sdn Bhd* [1984] 1 CLJ 219; [1984] 1 CLJ (Rep) 108; [1984] 1 MLJ 248; [1983] 1 MLRA 281 – where the Federal Court held, at pp. 114 & 118 (CLJ); pp. 252 and 255 (MLJ):

[at MLJ page 252] ...

... The Privy Council drew attention to the error implicit in the Special Commissioners expressing as findings of fact statements which are in truth propositions of law. The case stated in this appeal is open to similar criticism in a number of respects.

Appeals from the decisions of the Special Commissioners in tax cases are made by way of case stated under the Income Tax Act, 1967 Schedule 5, paragraph 34. The paragraph states clearly that any appeal is on a question of law. Hence, *pure findings of fact may not be challenged on an appeal. However, the court has clear and undoubted jurisdiction to reverse a decision on questions of law. The term "question of law" includes the correctness of (a) pure statements of law (e.g. as to the correct interpretation of a statutory provision), and (b) the inferring of a conclusion from the primary facts (where the process of inference involves assumptions as to the legal effect or consequences of the primary facts).*

In Chu Lip Kong's case [1982] 1 MLJ 235 the Privy Council reversed the Commissioners' decision on the ground that it was wrong in law. The approach is similar to that of the House of Lords in *Edwards v. Bairstow & Harrison* [1956] AC 14; [1955] 3 All ER 48; (1953) 36 TC 207, a case universally acknowledged as the leading authority on the distinction between questions of fact and questions of law. It was also referred to by the learned Judge. He was fully conscious of the critical distinction between questions of fact and law. He stated the position succinctly and accurately before citing a passage from the above case. At page 54 of the Appeal Record he reminded himself in the following words:

> *... The power of the court to interfere is quite limited where the findings of the Special Commissioners are basically findings of facts. The court will interfere only if there is no evidence to justify the finding or where they have applied erroneous tests in arriving at their conclusions or have drawn a wrong inference on the facts or have misdirected themselves in law ...*

[at MLJ page 255]

The question of what the statute means by "interest" is a question of law. However strong one may feel as to the facts one must remember the facts are for the decision of the Commissioners. The facts are not disputed either by the Taxpayer or the learned Judge. They accepted that *the finding of fact is not subject to appeal. But in this case it is not simply a question of fact. None of the matters is a question of fact on which the determination of the Commissioners is conclusive. All of them present questions of law which are open to review by the court on appeal ...*

(emphasis added)

A **The Requirements For A Reinvestment Allowance**

[23] To recapitulate – for the appellant to be entitled to an RA, the appellant has to fulfil these requirements:

(i) the appellant must have been in operation for "not less than 12 months", *ie*, at least 12 months before claiming the RA.

B

(ii) the appellant has spent money on a factory or machinery for the purpose of a qualifying project, which is a project to expand, modernise or automate its existing business, in manufacturing or processing a product or related product in the same industry.

C

(iii) alternatively, the appellant has spent money on a factory or machinery for the purpose of a project to diversify its existing business into any related product within the same industry.

[24] To "expand" is to increase product capacity, *ie*, to make more products, or to expand its factory area. To "modernise" is to upgrade its equipment and process. To "automate" is to substitute manual operations with mechanical operations with reduced human activity. To "diversify" is to increase, or even just to change, the taxpayer's range of products (but the products must relate to the same industry).

D

E **Considering The Appellant's Appeal**

[25] In considering this appeal, I am to analyse the SCIT's case cited, which contains the SCIT's grounds for its decision dismissing the appellant's appeal against the IRB's refusal to grant to the appellant the RA in YA 2006, and consequentially, the IRB's imposition of additional tax (penalty) for YA 2007 and YA 2008. In other words, the SCIT upheld the IRB's refusal to give the appellant the RA applied for, and instead assessed a penalty on the appellant.

F

[26] Further, I am to consider the appellant's appeal on questions of law. In this regard:

G

(i) it is a question of law whether the SCIT's finding – that the appellant did not satisfy the requirements to get the RA, *ie*, the appellant had not carried out a project of "expanding, modernising or automating its existing business" in respect of "processing" a product, and had not diversified (increased or changed its range of products) – was justified by the evidence.

H

(ii) it is a question of law whether the SCIT arrived at their decision through a misinterpretation of para. 8 of Schedule 7A of the ITA on what constituted a "qualifying project".

I

(iii) it is a question of law whether, on the balance of probabilities, the appellant has been "in operation for not less than 12 months" before it made the application for the RA, to satisfy the requirement under para. 1(a) of Schedule 7A.

Grounds For Allowing The Appellant's Appeal

The SCIT Misinterpreted Paragraph 8 Of Schedule 7A On The Meaning Of "Qualifying Project"

[27] In their case stated, the SCIT found that the appellant was not carrying out the activity of processing a product (here: the product is rice). The SCIT held that there was no evidence that the machinery that the appellant purchased "processed paddy into rice". The SCIT stated that the appellant's machinery sorted out the rice grains; the machinery merely sorted out the good rice grains from the blackish rice grains; the activity of sorting the rice grains simply ensured that the rice did not contain unwanted matter; and the sorting did not change the structure of the rice grains, like when paddy was processed to rice. In other words, the SCIT found that since the sorting activity performed by the appellant's machinery did not change the structure of the rice, such as turning paddy into rice – the appellant was not processing the rice. And since the appellant was not processing the rice, the appellant did not satisfy the processing requirement under para. 8(a) of Schedule 7A.

[28] With respect, the SCIT's reasoning is insupportable. First – the SCIT did not indicate the authority or at least the reference that instructed them to find that when an activity did not change the structure of the rice grains, the activity could not be considered to be the required "processing" activity under para. 8(a) of Schedule 7A. The SCIT appeared to have come up with that definition or description on their own.

[29] Paragraph 9 of Schedule 7A does not have a definition for "processing". Perhaps the SCIT had in mind the definition of the activity of "manufacturing", instead of "processing". Paragraph 9 of Schedule 7A defines "manufacturing" as a conversion of organic material into a new product "by changing the composition, nature or quality of such materials". Similar to what the SCIT described as changing the structure of the rice, like turning paddy into rice. But this definition (or description) concerns "manufacturing", and not "processing". And it was "processing" which figured prominently in the SCIT's case cited.

[30] I find that the SCIT had misdirected itself on the meaning of "processing" in the context of the requirements of para. 8(a) of Schedule 7A.

[31] Second – RA is allowed for "processing". Since para. 9 of Schedule 7A does not define "processing", I looked at the several definitions of "processing" submitted by both parties. The definition that is by far the most appropriately applicable for this appeal is found in the IRB's own Reinvestment Allowance Public Ruling No. 6/2012 dated 12 October 2012.

[32] It is apt to note that it was the appellant, and not the IRB, who referred to the IRB's own directly-applicable definition of "processing" in a claim for RA.

[33] The IRB's Reinvestment Allowance Public Ruling No. 6/2012, in para. 6.2.2, provides definitions for "processing" which include the following definitions (with my emphases added):

> (1) processing is the subjection of goods to a process which means, goods or materials are **subjected to a process** which falls short of the manufacturing of a new article **and involves the treatment of the goods in some way**, other than natural growth.
>
> (2) processing refers to **a technique of preparation, handling or other activity designed to effect a physical** or chemical change *in an article* or substance.
>
> (3) an activity may be termed as processing where a product has **gone through a series of actions that are systematic, has a higher value than before** (has been made more marketable and would attract a higher price for the same amount) and accepted by the market.
>
> (emphasis added)

[34] Third – the evidence discloses that the appellant's business, and by extension, the machinery that the appellant purchased (for which it is claiming an RA), is to turn raw rice into three products:

(i) processed rice (for household consumption);

(ii) broken rice (supplied to factories that make noodles, like vermicelli); and

(iii) rice bran (sold as animal feed).

[35] The appellant's machinery systematically subjects the raw rice to a series of actions that physically change the raw rice into these three products, which, when taken together, have a higher value than the raw rice in its original form. To my mind, it is clear and undoubtable that the appellant carried out the activity of "processing".

[36] Further, the appellant "expanded" its business by building a factory that is larger than its previously rented factory premises. The appellant "automated" its business by purchasing machinery, such as the various sorter machines (thus reducing human effort) to process the raw rice into the three different products.

[37] On the terms of paras. 1, 8(a) and 9 of Schedule 7A of the ITA, and in the context of the IRB's own definitions of "processing" – I find, with respect, that the SCIT had seriously misdirected themselves that the appellant did not carry out the activity of "processing", which led the SCIT to erroneously deny the appellant's claim for an RA.

The SCIT Wrongly Placed A Higher Burden Of Proof On The Appellant

[38] The SCIT placed a higher burden of proof on the appellant than was necessary when the SCIT required the appellant to prove that its business or its machinery changed "the structure of the rice", citing the example of turning paddy into rice, before the SCIT would accept that the appellant performed the required activity of "processing" the rice, to be entitled to make an RA claim.

[39] It is my view that the SCIT should have, instead, simply considered whether the appellant turned the raw rice into another form (into another product). That would have sufficed to hold that the appellant carried out the processing of rice.

[40] From case law, even the inspecting, the cutting-into-size, and the packaging of flowers were held to constitute the activity of processing – *Ketua Pengarah Hasil Dalam Negeri v. Classic Japan (M) Sdn Bhd & Another Appeal* [2021] 5 CLJ 86; [2021] 9 MLJ 870; [2021] 5 AMR 234; [2022] MLRAU 44.

[41] In *Classic Japan* (*supra*), the taxpayer was in the business of collecting, cutting-into-size, and shipping of the packaged flowers for export. The taxpayer claimed for an investment building allowance for the money spent to construct its factory. The High Court held that the handling of the flowers (cutting them into specific sizes, lengths and weights; storing them; and packaging them for export) qualified as subjecting the flowers to process, to entitle the taxpayer to claim the investment building allowance.

[42] Further, and more pertinently, case law instructs me that the RA claim in the ITA was implemented for the very purpose of encouraging companies to expand, modernise and automate their businesses, to increase their production capacities. As such, the provisions of Schedule 7A should be interpreted purposively and not restrictively – at the High Court: *Tenaga Nasional Bhd v. Ketua Pengarah Hasil Dalam Negeri* [2022] 7 CLJ 285; [2022] MLJU 396; [2022] AMEJ 0211; [2022] 5 MLRH 47; and on appeal to the Court of Appeal: *Ketua Pengarah Hasil Dalam Negeri v. Tenaga Nasional Bhd* [2024] 8 CLJ 301; [2024] 5 MLRA 129; [2024] MLJU 1039.

[43] In *Tenaga Nasional Bhd* (*supra*), the High Court held (with my emphasis added too):

> [16] The RA was introduced when Parliament passed the Income Tax (Amendment) Act 1979 (A451) on 1 March 1979 and *based on the "Penyata Rasmi Parlimen" Hansard* dated 13 December 1978, *RA was introduced into the ITA to encourage companies to have a modernisation plan to increase the production of the company*. The High Court in *Ketua Pengarah Hasil Dalam Negeri v. Marigold Industries (M) Sdn Bhd* [2018] MSTC 30-116 had stated:
>
> > Based on s. 17A of the Interpretation Acts 1948 and 1967 and the Federal Court's judgment in *Palm Oil Research and Development Board Malaysia & Anor v. Premium Vegetable Oils Sdn Bhd* (2005)

> MSTC 4, 098; [2004] 2 CLJ 265, *s. 133A, paras. 1 and 8(a) of Sch 7A should be given purposive interpretation. The purpose of s. 133A, read with paras. 1 and 8(a) of Sch 7A, was to provide a "special incentive relief" to companies resident in Malaysia which had been in operation for not less than 12 months, to invest in the expansion modernisation or automation of their product manufacturing or processing*.
>
> ...
>
> [52] *Schedule 7A ITA, including what amounts to qualifying project is not to be construed narrowly in the manner in which the respondent does as it tantamount to defeating the intention of Parliament in granting RA. The purposive approach in interpreting tax provisions have been recognised by our courts*. The Federal Court in *Palm Oil Research And Development Board Malaysia & Anor v. Premium Vegetable Oils Sdn Bhd* [2004] 2 CLJ 265; [2005] 3 MLJ 97 had held:
>
> > It is clear beyond doubt that in view of s. 17A of the Interpretation Acts 1948 and 1967 *there is now a statutory recognition for the courts to take purposive approach in the interpretation of statutes including taxing statutes*.
>
> (emphasis added)

[44] In *Tenaga Nasional Bhd* (*supra*), the Court of Appeal held (with my emphases added too):

> [74] Section 17A of the Interpretation Acts 1948 and 1967 states as follows:
>
> > *Regard to be had to the purpose of Act*
> >
> > 17A. *In the interpretation of a provision of an Act, a construction that would promote the purpose or object underlying the Act* (whether that purpose or object is expressly stated in the Act or not) *shall be preferred to a construction that would not promote that purpose or object*.
>
> [77] At the Parliamentary debate on 13 December 1978, this was said by the then Deputy Minister of Finance at pp. 4210 to 4211:
>
> > Di dalam Ucapan Belanjawan 1979, Yang Berhormat Mulia Menteri Kewangan telah juga mengemukakan cadangan untuk mengadakan galakan bagi perusahaan-perusahaan yang sudah bertapak dalam bentuk elaun pelaburan semula *untuk menggalakkan mereka mengadakan rancangan permodenan serta menambahkan pengeluaran ...*
>
> (emphasis added)

[45] I am guided and bound to take a purposive interpretation of the provisions under Schedule 7A for RA, which encourages company-taxpayers to expand, modernise and automate their manufacturing and processing, as well as to diversify their businesses, and which gives a proper effect to the legislative intent of Schedule 7A, instead of a restrictive or limiting

interpretation of Schedule 7A (which is what the SCIT had done). Particularly when the IRB does not dispute that the appellant had expended the capital expenditure for which it claimed an RA. The dispute was only about whether the appellant had spent the money for a qualifying project, to entitle it to an RA.

[46] By placing this higher burden of proof on the appellant, to prove, ever so narrowly, that the appellant changed "the structure of the rice", such as turning paddy into rice – the SCIT had misdirected themselves and misapplied the law.

The SCIT Disregarded The Evidence

[47] Among the documentary evidence produced by the appellant to support its claim for an RA, the appellant produced:

(i) an invoice dated 26 November 2002 issued by Agro-Industrial Supplies (M) Sdn Bhd to the appellant for the purchase of two units of the Toyo Super Coloured Grain Sorter (Double Sorting Type) for RM520,000;

(ii) a debit note dated 25 December 2005 issued by Ban Heng Bee Rice Mill (1952) Sdn Bhd (Ban Heng Bee) to the appellant for two units of Yamatech Grain Colour Sorter Double Sensor for RM655,424, and a related credit note dated 20 December 2005 issued by Ban Heng Bee to the appellant for the same machinery for RM30,000. The debit note and credit note both refer to Taiwan Yamakawa Technology Co Ltd's (Taiwan Yamakawa) Invoice No. 2005/031 dated 22 September 2005;

(iii) a commercial invoice dated 22 September 2005 issued by Taiwan Yamakawa "for the account and risk of" Ban Heng Bee, for three units of Yamatech Grain Colour Sorter Double Sensor for JPY29.4 million (JPY9.8 million each);

(iv) a debit advice dated 3 October 2005 issued by United Overseas Bank (Malaysia) Bhd to Ban Heng Bee, debiting RM983,681.44 (the Ringgit equivalent of JPY29.4 million from Ban Heng Bee's account) for the three units of machinery purchased from Taiwan Yamakawa. On the debit advice, there was a note stating that three units of the machinery cost RM983,681.44, then two units of the machinery, which was sold onwards to the appellant, would cost RM655,424 (approximated by 2/3 x RM983,681.44);

(v) a brochure and a user's manual for the Yamatech Grain Colour Sorter machinery.

[48] The SCIT accepted that the appellant purchased the Toyo Super Coloured Grain Sorters in 2002 because the invoice for the two units of that machine was issued to the appellant.

[49] The SCIT, however, refused to accept that the appellant purchased two units of the Yamatech Grain Colour Sorter Double Sensor machines in 2005 because:

(i) the brochure and the user's manual – which showed that the function of the subject machinery is to process rice – are for the Yamatech machines (not the Toyo machines);

(ii) but the Yamatech machines were purchased by Ban Heng Bee (not by the appellant); the invoice issued by Taiwan Yamakawa was to Ban Heng Bee (and not to the appellant);

(iii) all three Yamatech machines could only be Ban Heng Bee's machines (and not the appellant's machines).

[50] Put differently: concerning the Toyo machines – the SCIT accepted that the appellant purchased the Toyo machines. But the appellant did not produce a brochure or user's manual for the Toyo machines, to prove that the Toyo machines process rice. So, the SCIT decided that purchasing the Toyo machines did not prove that the appellant processed rice.

[51] Concerning the Yamatech machines-the SCIT accepted that the brochure and user's manual prove that the Yamatech machines process rice. Capital expenditure to purchase the Yamatech machines would entitle the appellant to an RA. But the SCIT decided that the appellant did not purchase the Yamatech machines. It was Ban Heng Bee who purchased the Yamatech machines. Hence, the SCIT decided that the appellant cannot use the purchase of the Yamatech machines to claim RA.

[52] And so, the SCIT rejected the appellant's claim for RA on these superficial grounds.

[53] The SCIT arrived at these grounds through a serious misdirection and misapplication of the law on evidence because the SCIT ignored (disregarded) all the other relevant evidence. The SCIT disregarded:

(i) the evidence that the appellant purchased two units of the Yamatech machines through Ban Heng Bee. The evidence – documentary evidence and oral evidence from AW1/appellant's director-witness – unequivocally demonstrates that Ban Heng Bee purchased three units of the Yamatech machine from Taiwan Yamakawa. Ban Heng Bee paid for the three machines. Then Ban Heng Bee sold onwards two units of the Yamatech machines to the appellant. Ban Heng Bee issued a debit note for the price of the two machines to the appellant, against the appellant's account with Ban Heng Bee. The appellant clearly incurred capital expenditure to acquire the two Yamatech machines; and

(ii) the evidence from AW1 (appellant's director-witness) that both the Toyo machine and the Yamatech machine performed the same function, which was to sort and clean the raw rice. Even the name and description of both machines are the same. The Toyo machine is called the Coloured Grain Sorter, while the Yamatech machine is called the Grain Colour Sorter. Both machines sort rice. It is not unreasonable to infer that the brochure and user's manual for the Yamatech machine also disclose how the Toyo machine also processes rice.

[54] On another aspect about disregarding the evidence, the SCIT erroneously (in my view) required the appellant to prove that it had been performing processing activity for not less than 12 months (menjalankan aktiviti pemprosesan tidak kurang dari tempoh 12 bulan: see para. 10.8 of the case cited). I do not comprehend the source of this requirement.

[55] Paragraph 1 of Schedule 7A requires that for the appellant to be eligible for RA, the appellant must have "been in operation for not less than 12 months". There is no requirement for the appellant to have been performing processing activity for not less than 12 months before making a claim for RA. The SCIT could only have arrived at this purported requirement through a misdirection and a misinterpretation of para. 1 of Schedule 7A.

[56] In this regard, the SCIT disregarded the evidence that shows that the appellant had been in operation for longer than 12 months before the YA 2006. The SCIT omitted to consider or disregarded:

(i) the evidence that the appellant was incorporated in 1995;

(ii) the November 2002 invoice (dated 26 November 2002) for the appellant's purchase of the Toyo Super Coloured Grain Sorter;

(iii) the March 2001 invoice (dated 17 March 2001) for the appellant's purchase of the shining machine;

(iv) the July 2001 invoice (dated 7 July 2001) for the appellant's purchase of the vibrator separator machine;

(v) the August 2001 invoice (dated 7 August 2001) for the appellant's purchase of the auto packer machine;

(vi) the August 2001 invoice (dated 19 August 2001) for the appellant's purchase of the destoner machine.

[57] Another instance where the SCIT disregarded the relevant evidence and misdirected themselves on the interpretation of para. 1 of Schedule 7A was when the SCIT insisted that for the appellant to be given the RA, there is a requirement that the appellant must have been operating a rice processing business at least 12 months before it made the RA claim.

[58] The appellant's tax agent (by letter dated 27 April 2012) informed the IRB that before 2006, the appellant was a rice wholesaler, and in 2006, it diversified into the business of processing raw rice (into processed rice, broken rice and rice brand). The IRB rejected the appellant's claim for an RA because the IRB surmised that if the appellant was a mere wholesaler in 2006, then the appellant would have started its rice processing business less than 12 months from the time that the appellant made an RA claim in YA 2006.

[59] The tax agent later informed the IRB that it was his mistake to have stated that the appellant started its rice processing business only in 2006. The appellant's tax agent clarified with the IRB that the appellant had actually been in the rice processing business eight years before YA 2006. To support this assertion, the tax agent produced supporting documents to prove that the appellant had been in the rice processing business for much longer than 12 months before YA 2006. Despite the clarification, which was supported by documentary evidence, the IRB rejected the tax agent's clarification as well as the documentary evidence.

[60] I can see no good reason for the IRB to reject the tax agent's clarification and the appellant's supporting documents.

[61] The SCIT omitted to consider this evidence. The SCIT insisted on holding that the appellant had failed to prove that it had been in the rice processing business for more than 12 months before it made the RA claim in 2006.

[62] In any event, I find that there is no requirement that for the appellant to be given the RA claim, the appellant had to have been in the rice processing business for at least 12 months before it made the RA claim. The 12-month requirement was merely for the appellant to have been in operation for at least 12 months when it made the RA claim.

The SCIT Misinterpreted The Law On The Appellant's Wholesale Licence

[63] The SCIT stated that since the appellant held a wholesale licence, the appellant could not be processing rice or be allowed to process rice. The appellant could only be a rice wholesaler. And if the appellant did not have a licence to process rice, it could not be entitled to an RA for expanding its factory and purchasing machinery for the business of rice processing.

[64] There was, however, no relevant provision that prohibited a licenced wholesaler like the appellant from processing rice. The appellant's wholesale licence was governed by the Control of Padi and Rice (Licensing of Wholesalers and Retailers) Regulations 1996 (Licensing Rules). Under the Licensing Rules, the appellant was particularly subjected to the duties of a wholesale licensee set out in reg. 8 and reg. 9 of the Licensing Rules.

[65] Regulation 8 and reg. 9 obligated the appellant to perform certain duties and prohibited the appellant from performing certain acts. But these regulations did not prohibit the appellant from operating a rice-processing business.

[66] And so, I find that there was no basis in law for the SCIT to have found that the appellant could not be allowed to carry out rice processing, and hence could not be given the RA claimed because the RA related to a prohibited activity.

[67] Regulations 8 and 9 are set out below for reference:

Regulation 8. General duties of licensee.

A licensee:

(a) shall not store or keep, or permit to be stored or kept, any rice except at the business premises or stores specified in the licence; and

(b) shall not hoard, conceal or destroy rice.

Regulation 9. Special duties of wholesale licensee.

(1) A wholesale licensee who is also a rice miller:

(a) shall not acquire, purchase or sell any rice except the rice which has been milled or the padi purchased by him under a licence issued to him in accordance with the Control of Padi and Rice (Licensing of Padi Purchasers) Regulations 1996 [P.U.(A) 625/96]; and

(b) shall not sell any rice to any person except to a wholesale licensee who is not a rice miller, a retail licensee, any person who requires rice for the purposes of the manufacturing or catering business and any supplier of rice under contract.

(2) A wholesale licensee who is not a rice miller:

(a) shall not acquire or purchase rice from any source except through imports approved by the Government or through Government tenders or other wholesale licensees who are also licensed millers; and

(b) shall not sell rice to any person except to a wholesale licensee who is not a rice miller, a retail licensee, any person who requires rice for the purposes of the manufacturing or catering business and any supplier of rice under contract.

(3) A wholesale licensee shall maintain a day to day account of all purchases of rice or of rice recovered through milling, the total sales and stock-in-hand and the accounts shall be made available to any authorised officer for his inspection at the business premises if requested.

(4) A wholesale licensee who is involved in the packaging of rice shall exhibit a label or tag indicating the grade, weight, price, name, licence number and the percentage of broken rice on the package or container of the rice.

(5) Any sale of rice shall be accompanied by an invoice bearing the following particulars:

(a) name of business;

(b) the address of the business premises;

(c) the licence number;

(d) the date of sale;

(e) the name and address of the purchaser;

(f) the number of the wholesale or retail licence;

(g) if the purchaser is not a wholesale licensee or a retail licensee, the nature of the business establishment; and

(h) the country of origin, quality, price and total value of the rice sold.

Penalty And Additional Tax

[68] The SCIT held that since the appellant did not qualify for RA, the IRB rightly imposed penalties under ss. 112(3) and 113(2) of the ITA, amounting to RM21,012.24 for YA 2007, and RM542,505.26 for YA 2008.

[69] The appellant has paid these amounts to the IRB. The appellant prays that if this court finds that it is entitled to the RA, the penalties should not have been imposed. Then, these amounts should be ordered to be returned to the appellant.

Conclusion

[70] For the reasons stated above, I allow the appellant's appeal, set aside the SCIT's deciding order dated 27 March 2018, and discharge the IRB's (respondent's) assessments concerned, with costs of RM15k to be paid by the IRB (respondent) to the appellant.

[71] I also order the penalty amounts of RM21,012.24 for YA 2007, and RM542,505.26 for YA 2008, which were already paid over by the appellant to the IRB (respondent), to be returned by the IRB (respondent) to the appellant.